

Message Text

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ACTION EB-08

INFO OCT-01 EUR-12 IO-13 ISO-00 AGRE-00 CEA-01 CIAE-00
COME-00 DODE-00 FRB-03 H-01 INR-10 INT-05 L-03
LAB-04 NSAE-00 NSC-05 PA-01 CTME-00 AID-05 SS-15
STR-07 ITC-01 TRSE-00 ICA-11 SP-02 SOE-02 OMB-01
DOE-15 EA-10 XMB-02 /138 W
-----041757 251332Z /42

R 242215Z JUL 78
FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC 8163
INFO USMISSION GENEVA
AMCONSUL MONTREAL
AMCONSUL TORONTO
AMEMBASSY PARIS

C O N F I D E N T I A L OTTAWA 3683

PASS TREASURY FOR HUFBAUER

USMTN USOECD

E.O. 11652: GDS
TAGS: ETRD, EINV, CA
SUBJECT: TALKS ON AUTO INVESTMENT INCENTIVES AND DUTY
REMISSIONS

REF: OTTAWA (A) 3522 AND (B) 3459

1. SUMMARY: TREASURY DEPUTY ASSISTANT SECRETARY HUFBAUER
EXPRESSED CONCERN AND ALARM TO GOC OFFICIAL JULY 21 OVER
REPORTS OF DIRECT FEDERAL INVESTMENT SUBSIDIES OFFERED TO
FORD. HE ALSO EXPRESSED STRONG CONCERN OVER DUTY REMIS-
SION ARRANGEMENT BETWEEN GOC AND VOLKSWAGEN. GOC OFFI-
CIALS RESPONDED THAT INCENTIVES WERE IN RESPONSE TO IN-
CENTIVES OFFERED BY U.S. STATES. THEY ALSO MENTIONED
INCENTIVES OFFERED BY U.S. FEDERAL GOVERNMENT. HOWEVER,
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CANADIANS INDICATED EQUAL CONCERN WITH COMPETITIVE BIDDING
BY GOVERNMENTS FOR NEW INVESTMENT. THEY ALSO DEFENDED
DUTY REMISSION SCHEME AS NOT INCONSISTENT WITH GATT AND
IMPORTANT TO CANADA AS MEANS OF MAINTAINING SHARE OF NORTH
AMERICAN AUTOMOTIVE PRODUCTION. OFFICIALS EXPRESSED
WILLINGNESS TO CONSULT WITH U.S. ON WIDE RANGE OF ISSUES
AFFECTING NORTH AMERICAN AUTO INDUSTRY. HUFBAUER INDICA-

TED OUR CONCERNS ALSO MAY BE RAISED IN WASHINGTON WITH CANADIAN AMBASSADOR. END SUMMARY.

2. TREASURY DEPUTY ASSISTANT SECRETARY HUFBAUER SAID HE WISHED TO EXPRESS CONCERN AND ALARM OVER REPORTS ON DIRECT INVESTMENT SUBSIDIES OFFERED BY CANADIAN GOVERNMENT TO THE FORD MOTOR COMPANY. CANADIAN OFFICIALS, LEAD BY ROBERT JOYCE, ASSISTANT DEPUTY MINISTER OF FINANCE FOR INTERNATIONAL TRADE AND FINANCE, CONFIRMED THAT OFFER TO FORD INCLUDED DIRECT CASH PAYMENTS BY THE FEDERAL GOVERNMENT OF ABOUT HALF OF SOME CDOLS 75 MILLION TOTAL. FEDERAL OFFICIALS UNDERSTAND THAT FORD WILL RESPOND NEAR FUTURE.

3. HUFBAUER SAID WE RECOGNIZE THAT STATE AND PROVINCIAL GOVERNMENTS UNFORTUNATELY VIE TO LURE INDUSTRY BY OFFERING INVESTMENT INCENTIVATES, BUT HE SAID WE REGARD THIS FEDERAL INCENTIVE AS A NEW DEPARTURE WHICH VIOLATES SPIRIT AND COMES CLOSE TO VIOLATING LETTER OF THE U.S./CANADA AUTO AGREEMENT, ESPECIALLY ARTICLE 1, PARA. 1. HE ALSO SAID THE OECD INVESTMENT CODE, WHILE VAGUE ON MANY OF ITS DETAILS, WITH REGARD TO INCENTIVES AND DISINCENTIVES, CALLS FOR CONSULTATIONS IN SUCH CASES.

4. JOYCE SAID GOC SHARES CONCERN RE COMPETITIVE BIDDING BY GOVERNMENTS FOR NEW INVESTMENTS. IN THE FORD CASE, CONFIDENTIAL

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HOWEVER, GOC WAS RESPONDING TO INCENTIVES OFFERED BY U.S. STATES, AND FELT THAT SOME ACTION ON CANADIAN SIDE WAS REQUIRED. HE SAID THAT WHETHER ACTION HAPPENDED TO BE TAKEN BY FEDERAL OR PROVINCIAL GOVERNMENT DID NOT MAKE MUCH DIFFERENCE.

5. HUFBAUER NOTED THAT FEDERAL SUBSIDIES GREATLY ENLARGED POTENTIAL MAGNITUDE AND SCOPE FOR INVESTMENT INCENTIVES AND WERE CONTRARY TO AGREEMENTS BETWEEN FEDERAL GOVERNMENTS. GOC OFFICIALS NOTED THAT CANADIAN JUNIOR GOVERNMENTS WERE AT A DISADVANTAGE IN BIDDING AGAINST LARGER U.S. COUNTERPARTS.

6. GOC OFFICIALS ALSO NOTED PRESS REPORTS OF INVESTMENT SUBSIDY BY ECONOMIC DEVELOPMENT AGENCY OF U.S. COMMERCE DEPARTMENT FOR INVESTMENT PROJECT BY CHRYSLER IN TRENTON, MICHIGAN. IN RESPONSE TO A QUESTION, THEY DID NOT INDICATE THEY HAD ANY EVIDENCE THAT CHRYSLER WAS CONSIDERING ANY CANADIAN ALTERNATIVE IN TRENTON INVESTMENT.

7. HUFBAUER ASKED ABOUT REPORTS OF PLANNED INVESTMENT

INCENTIVES FOR GENERAL MOTORS PLANT IN QUEBEC. GOC OFFICIALS CONFIRMED FEDERAL INCENTIVE WAS UNDER CONSIDERATION, BUT NOTED IT WOULD BE GIVEN BY DEPARTMENT OF REGIONAL ECONOMIC EXPANSION (DREE) WHICH SEEKS TO LIMIT REGIONAL ECONOMIC DISPARITIES, AND THAT DREE GRANT WAS BEING CONSIDERED IN RESPONSE TO APPLICATION BY GM. THEY SAID FEDERAL INVESTMENT INCENTIVES HAD TO TAKE INTO CONSIDERATION REGIONAL PROBLEMS AND COMPETITION AMONG PROVINCES (READ: BETWEEN ONTARIO AND QUEBEC). THEY CONFIRMED THAT MICHELIN TIRE CASE HAD ALSO INCLUDED GRANT FROM DREE AS WELL AS FROM PROVINCIAL GOVERNMENT.

8. VW DUTY REMISSION. HUFBAUER SAID WE HAD ALWAYS
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CONSIDERED GATT 1960 WORKING REPORT, PARA. D., AS REQUIRING PHYSICAL TRACING OF PARTS ON WHICH DUTY COULD BE REMITTED. AN INTERPRETATION OF THE GOC-VW DUTY REMISSION AGREEMENT AS CONSISTENT WITH PARA. D. IS A GUTTING OF THAT REPORT.

9. GOC OFFICIALS SAID DUTY REMISSION AGREEMENT WAS NON-DISCRIMINATORY AS IT WAS DESIGNED BASICALLY TO GET PART OF NORTH AMERICAN AUTO PARTS PRODUCTION BY VW LOCATED IN CANADA, PROPORTIONAL OR POSSIBLY SLIGHTLY MORE THAN PROPORTIONAL TO THE SIZE OF THE CANADIAN MARKET. THE INCENTIVE WAS NEEDED TO INDUCE VW TO SOURCE PARTS IN CANADA. GOC OFFICIAL SAID THEY BELIEVE THIS APPROACH IS TO THE ADVANTAGE OF BOTH CANADA AND THE U.S. RATHER THAN UNECONOMIC AUTO ASSEMBLY OPERATIONS IN CANADA SUCH AS BY VOLVO AND RENAULT. THEY SAID THAT SIMILAR EMISSION SCHEMES MIGHT BE USED FOR POSSIBLE FUTURE AUTO ASSEMBLY OPERATION IN NORTH AMERICAN BY EUROPEAN OR JAPANESE PRODUCERS.

10. JOYCE SAID GOC RECOGNIZED THAT DUTY REMISSION SCHEME MIGHT LEAD TO COMPLAINTS AND EVEN COUNTERVAILING ACTION, BUT THAT THAT REMAINS TO BE SEEN.

11. JOYCE SAID ISSUES RAISED GO TO THE HEART OF THE AUTO AGREEMENT. HE RECOGNIZED THERE IS A DIFFERENCE OF VIEWS. GOC IS CURRENTLY UNDER POLITICAL PRESSURE FROM AUTO PARTS PRODUCERS TO BRING PARTS TRADE INTO BETTER BALANCE. HE DID NOT DISAGREE WITH HUFBAUER'S STATEMENT THAT "EQUITABLE" ASPECT OF PACT DID NOT NECESSARILY MEAN BALANCE, ESPECIALLY IN ALL ASPECTS OF AUTO TRADE, BUT JOYCE SAID GRAVE POLITICAL PROBLEMS WERE PRODUCED WHEN IMBALANCES GET TOO LARGE OR LAST TOO LONG.
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12. JOYCE SAID HE DID NOT ADVOCATE REOPENING THE AUTO AGREEMENT. THAT COULD LEAVE BOTH SIDES WORSE OFF. HOWEVER, HE THOUGHT WE MIGHT BUILD ON IT, POSSIBLY IN THE MTN. HE SIAD GOC HAD SUGGESTED LAST YEAR THAT U.S. AND CANADA MIGHT DISCUSS HOW THEY COULD DEVELOP COMMON APPROACH RE AUTOS IN GATT NEGOTIATIONS. SPEAKING PERSONNALLY, JOYCE SAID HE WOULD FAVOR SOME "COMING TOGETHER" BETWEEN CANADA AND THE U.S. ON HOW THE AUTO AGREEMENT WAS WORKING, INCLUDING QUESTION SUCH AS HOW THE NORTH AMERICAN INDUSTRY SHOULD APPROACH INCREASED PARTS IMPORTS FROM DEVELOPING COUNTRIES.

13. COMMENT.

A. WHILE GOC OFFICIALS SAID INCENTIVES OFFERED BY STATE OF OHIO TO FORD WAS "SUBSTANTIAL", WE UNDERSTAND THAT MOST OF INVESTMENT INCENTIVE OFFERED FORD WAS TO COMPENSATE FOR DIFFERENTIAL START UP COSTS IN ONTARIO (LAND ACQUISITION, MATERIAL, TAXES) HIGHER THAN ALTERNATIVE OF EXPANDING FORD PLANT IN OHIO. SEE REF. B)

B. POLITICAL PRESSURES ON PROVINCIAL AND FEDERAL GOVERNMENT FROM SOUTHWEST ONTARIO FOR MORE AUTO INVESTMENT AND PARTS EXPORTS DO EXIST, BUT WE ALSO NOT THAT IN HIS CONVERSATION WITH AMBASSADOR AND SENATOR BAYH JULY 4, (SEE OTTAWA 3459) PRIME MINISTER TRUDEAU SAID POLITICAL PRESSURE ON THE FEDERAL GOVERNMENT AS A RESULT OF THE PACT IS NOT OVERWHELMING.

C. GOC DESIRES FOR CONSULTATIONS WITH U.S. ON OPERATION OF NORTH AMERICAN AUTO INDUSTRY, WHICH HAVE BEEN MENTIONED TO US INFORMALLY AT GOC STAFF LEVEL HERE SEVERAL TIMES IN RECENT MONTHS, COULD INCLUDE NUMBER OF BOARD QUESTIONS OF INTEREST TO GOC. WE SHOULD BE AWARE THAT CANADIAN OBJECTIVE IN SUCH CONSULTATIONS ARE IN PART
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TO ALTER OPERATION OF THE AUTO PACT SO AS TO FURTHER THEIR OBJECTIVES OF TRADE AND INVESTMENT BALANCE.
ENDERS

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 jan 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: AUTOMOTIVE INDUSTRY, INVESTMENTS, SUBSIDIES
Control Number: n/a
Copy: SINGLE
Draft Date: 24 jul 1978
Decaption Date: 01 jan 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 20 Mar 2014
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1978OTTAWA03683
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Expiration:
Film Number: D780304-0957
Format: TEL
From: OTTAWA
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1978/newtext/t19780727/aaaaawvr.tel
Line Count: 220
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: fa31f96d-c288-dd11-92da-001cc4696bcc
Office: ACTION EB
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 5
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: 78 OTTAWA 978
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 08 jul 2005
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 1907917
Secure: OPEN
Status: NATIVE
Subject: TALKS ON AUTO INVESTMENT INCENTIVES AND DUTY REMISSIONS
TAGS: ETRD, EINV, CA
To: STATE
Type: TE
vdkgvwkey: odhc://SAS/SAS.dbo.SAS_Docs/fa31f96d-c288-dd11-92da-001cc4696bcc
Review Markings:
Sheryl P. Walter
Declassified/Released
US Department of State
EO Systematic Review
20 Mar 2014
Markings: Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014